

ORIGINAL



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MEMORANDUM

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TO: Docket Control

FROM: Ernest G. Johnson
Director
Utilities Division

EA for EGJ

DATE: April 19, 2005

RE: STAFF REPORT FOR TIME WARNER TELECOM OF ARIZONA LLC,
AUTHORIZATION TO GUARANTEE DEBT OF A PARENT
CORPORATION (DOCKET NO. T-03943A-05-0070)

Attached is the Staff Report for Time Warner Telecom of Arizona, application for authorization to guarantee debt of its parent. Staff recommends approval.

EGJ:JHJ:red

Originator: J. H. JOHNSON

Attachment: Original and sixteen copies

Arizona Corporation Commission
DOCKETED

APR 18 2005

DOCKETED BY	<i>CA</i>
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AZ CORP COMMISSION
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Docket No. T-03943A-05-0070

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**STAFF REPORT
UTILITIES DIVISION
ARIZONA CORPORATION COMMISSION**

**TIME WARNER TELECOM
OF ARIZONA LLC**

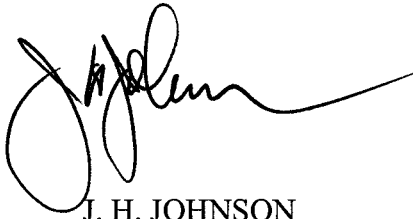
DOCKET NO. T-03943A-05-0070

**APPLICATION FOR AUTHORIZATION
TO GUARANTEE DEBT**

APRIL 2005

STAFF ACKNOWLEDGMENT

The Staff Report for Time Warner Telecom of Arizona LLC, Docket No. T-03943A-05-0070 was the responsibility of the Staff member listed below: J. H. Johnson was responsible for the review and financial analysis of the Company's application.

A handwritten signature in black ink, appearing to read 'J. H. Johnson', with a large loop on the left and a long horizontal stroke extending to the right.

J. H. JOHNSON
PUBLIC UTILITIES ANALYST III

EXECUTIVE SUMMARY

Time Warner Telecom of Arizona LLC ("TWTA") filed an application with the Arizona Corporation Commission ("Commission") on February 3, 2005, asking authorization to guarantee the debt of its parent, Time Warner Telecom Holdings ("TWT Holdings") in an amount up to and including \$400,000,000 of 9.25 percent Senior Notes.

TWTA is a limited liability company organized and existing under the laws of the State of Delaware. TWTA operates in Arizona with 38 employees serving approximately 350 commercial and governmental accounts.

TWTA is a subsidiary of TWT Holdings which in turn is a wholly owned subsidiary of Time Warner Telecom Inc.

The purpose of the financing requested is to re-issue existing Senior Notes to extend the maturity of the notes from 2008 to 2014 and save \$2 million per year in interest expense.

The change in the interest expense has no effect on the times interest earned ratio but nudges the debt service coverage ratio from 1.72 to 1.75 for the parent organization.

The capital structure does not change as a result of the re-issuance of the notes. Time Warner Telecom, Inc. remains a highly leveraged entity with long term debt equaling 77.2 percent of the capital structure. Concerns over Time Warner Telecom Inc.'s highly leveraged capital structure are mitigated by the alternative providers for service should it have service consequences for customers.

Staff considers that the guarantee of TWT Holdings debt by TWTA is in the public interest due to interest savings and maturity extension and is unlikely to have any effect on Arizona customers of TWTA.

Staff recommends the approval of TWTA's request for authorization to guarantee the \$400,000,000 debt of TWT Holdings on the terms and conditions described in the application.

TABLE OF CONTENTS

	<u>PAGE</u>
INTRODUCTION	1
NOTICE	1
BACKGROUND.....	1
PURPOSE OF FINANCING.....	1
DESCRIPTION OF PROPOSED FINANCING	1
FINANCIAL ANALYSIS	2
COMPLIANCE	2
STAFF CONCLUSIONS AND RECOMMENDATIONS.....	2

SCHEDULE

SELECTED FINANCIAL DATA.....	Schedule JHJ -1
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Introduction

Time Warner Telecom of Arizona LLC ("TWTA") filed an application with the Arizona Corporation Commission ("Commission") on February 3, 2005, asking authorization to guarantee the debt of its parent, Time Warner Telecom Holdings ("TWT Holdings") in an amount up to and including \$400,000,000 of 9.25 percent Senior Notes.

Notice

TWTA's customer base in Arizona is all governmental and commercial customers so Notice is not necessary.

Background

TWTA is a limited liability company organized and existing under the laws of the State of Delaware. TWTA operates in Arizona with 38 employees serving approximately 350 commercial and governmental accounts.

TWTA is a subsidiary of TWT Holdings which in turn is a wholly owned subsidiary of Time Warner Telecom Inc.

Further, TWTA is certificated by the Arizona Corporation Commission to provide competitive intrastate telecommunications services pursuant to Decision No. 63262.

Purpose of Financing

The purpose of the TWT Holdings financing is to re-issue existing Senior Notes to extend the maturity of the notes from 2008 to 2014. The transaction contemplates an interest savings of 0.50 percent. The projected change in the interest rate as filed amounts to an interest savings of \$2 million per each year the Senior Notes are outstanding.

Description of Proposed Financing

TWT Holdings plans to re-issue up to \$400 million in 9.25 percent Senior Notes maturing in 2014 with proceeds to be used to redeem TWT Holdings 9.75 percent Senior Notes due in 2008.

The refinancing requires that each state level operating subsidiary, including TWTA, guarantee the obligation under the notes. No pledge of assets is required.

Financial Analysis

Staff performed no financial analysis of the state operating subsidiary because no change is expected in TWTA's operating results due to the re-issuance of debt by TWT Holdings.

Staff prepared Schedule JHJ-1 (attached) using information from Time Warner Telecom, Inc.'s Form 10-K. The pro forma information shows the impact of the anticipated \$2 million per year interest savings. The change in the interest expense has no effect on the time interest earned ratio ("TIER"), but nudges the debt service coverage ratio ("DSC") up from 1.72 to 1.75.

The Debt Service Coverage ratio ("DSC") represents the number of times internally generated cash will cover required principal and interest payments on long-term debt. A DSC greater than 1.0 indicates that operating cash flow is sufficient to cover debt obligations.

The Times earned Interest Ratio ("TIER") represents the number of times earnings will cover interest expense on long-term debt. A TIER greater than 1.0 means that operating income is greater than interest expense. A TIER less than 1.0 is not sustainable in the long term but does not necessarily mean that debt obligations cannot be met in the short term.

The capital structure does not change as a result of the re-issuance of the notes. Time Warner Telecom, Inc. remains a highly leveraged entity with long term debt equaling 77.2 percent of the capital structure. Concern over Time Warner Telecom Inc.'s highly leveraged capital structure are mitigated by the alternative providers for service should it have service consequences for customers.

Compliance

There are no compliance delinquencies for this company.

Staff Conclusions and Recommendations

Staff concludes that the guarantee in support of an affiliates financing is within the corporate powers of TWTA, compatible with the public interest, and will not impair its ability to perform service.

Staff further concludes that authorization is warranted because the refinancing extends maturities on debt obligations resulting in enhanced ability to repay existing debt.

Staff recommends the approval under AAC R-14-2-804(B) of TWTA's request for authorization to guarantee the debt of TWT Holdings of \$400,000,000 on the terms and conditions described in the application.

Staff further recommends approval of granting of liens in favor of the lender as required to secure the borrowings authorized.

Staff further recommends authorizing TWTA to engage in any transaction and to execute any documents necessary to effectuate the authorizations granted.

FINANCIAL ANALYSIS

Selected Financial Data
From the December 31, 2004 Form 10-K Filing with the Securities and Exchange Commission
(000's)

		[A] 12/31/2004		[B] Pro Forma	
1	Operating Income	\$ (17,203)		\$ (17,203)	
2	Depreciation & Amort.	230,688		230,688	
3	Income Tax Expense	0		0	
4					
5	Interest Expense	122,391		120,391	
6	Repayment of Principal	1,387		1,387	
7					
8					
9	TIER				
10	[1+3] ÷ [5]	-0.14		-0.14	
11	DSC				
12	[1+2+3] ÷ [5+6]	1.72		1.75	
13					
14					
15					
16					
17					
18	Short-term Debt	\$1,387	0.1%	\$1,387	0.1%
19					
20	Long-term Debt	\$1,249,197	77.2%	\$1,249,197	77.2%
21					
22	Common Equity	\$367,158	22.7%	\$367,158	22.7%
23					
24	Total Capital	\$1,617,742	100.0%	\$1,617,742	100.0%
25					
26					
27					